

**THREE-TIER
SYSTEM
REVIEW PANEL
MATERIALS
(1999)**

DEFENDANT'S EXHIBIT	
CASE NO.	C04-0360P
EXHIBIT NO.	534



STATE OF WASHINGTON
WASHINGTON STATE LIQUOR CONTROL BOARD
3000 Pacific Ave SE • PO Box 43075 Olympia WA 98504-3075 • (360) 664-1648

August 25, 1999

Charles Smarr
Brydon, Swearingen, and England
312 E Capital Ave
Jefferson City, Missouri 65102

Dear Mr. Smarr,

Following is an outline of the Washington State Liquor Control Board's three tier system review panel, which was convened on November 19, 1999.

Why conduct a review of the three tier system?

Washington State's system for the post-Prohibition regulation of alcohol was set in place by the legislature in 1934 in the Steel Act, which both legalized the sale of alcohol and established a three tier system separating manufacturing, wholesaling, and retailing from one another. This basic structure still forms the "backbone" of the licensing and regulation structure.

The complexity of corporate organization has increased considerably since 1934, due especially to the emergence of the multi-purpose corporation which owns and operates a variety of disparate enterprises. Every recent legislative session has considered proposals intended to make exceptions to the three tier system, many of which have been enacted. The changing business atmosphere coupled with the growing impact of electronic technologies will continue to bring challenges to this policy.

For these reasons, the Washington State Liquor Control Board has been conducting a review of the three tier system. The recommendations from this review will be available for consideration in the legislature that will convene in the year 2000.

What is the role of the advisory panel?

To assist the Liquor Control Board in the formulation of recommendations and in order to provide for an open, informed debate, the Board convened an advisory panel that includes members representing the groups listed below. Wherever an association represents these interests, the appropriate association was asked to name the representatives.

Manufacturers (3)
Retailers (2)
Licensed Beverage Association
Legislators (4)

Beer and Wine Distributors (2)
Restaurant Association of Washington
General Interest (3)

TX534-002

What areas of discussion:

1. Is there any need for a change in the law?

The discussion leading to the formation of the review panel resulted from the continuing recurrence of legislative measures that provide exceptions to the Tied House law (RCW 66.28.010) – almost one exception per session in recent years. Nevertheless, some may view this as appropriate because it makes change more difficult and limits alterations to very specific circumstances.

2. Should there be a major change in the three tier system?

Does Washington State need to retain the three tier system or should this entire regulatory structure be replaced with something else? Should the panel want to explore such a major change, it would be appropriate for the group to consider at least the following:

- What would replace the existing system?
- How, as a practical matter, could change be achieved, given the need for legislative approval?

3. Should there be a revision to the Tied House law that permits the Liquor Control Board to rule on *de minimus* overlapping ownership?

Recent legislative sessions have witnessed a series of legislative proposals to legalize ownership arrangements that would have prevented acquisition of retail licensing under the current Tied House statute. Should the panel seek to frame a recommendation that would permit the Liquor Control Board to deal with these exceptional situations?

A generic change like the above could be combined with limitations on the total gross annual retail revenues that could be derived from the sale of products manufactured by the interest in question. This limit is set at 10% of total alcohol sales in Illinois and Georgia. New Jersey law includes a 5% limitation on stock ownership.

What about requiring some form of special reporting where exceptions are granted?

4. Should we reevaluate the exceptions already granted by the legislature?

Any proposed changes in the existing law need to be evaluated in order to prevent disruption of existing exceptions. (Or, we could go back and reevaluate the exceptions.)

Alternatively, should the exemptions already in law be included in any change or should they be eliminated in statute? If added limitations are included in a new statute, should existing exemptions be required to comply?

5. Should state law permit other economic arrangements between wholesalers and retailers?

For example:

- Should credit arrangements be permitted within certain time limits?
- Should joint advertising campaigns be permitted?
- Should a holder of a manufacturers license be permitted to be a lease holder for a retail licensee?
- Can we draw a clearer line regarding what is a "novelty item" (prohibited) and what is a point of sale advertisement (permitted)?

6. What kind of enforcement should be done relative to the tied-house law?

For example, should there be a more systematic inspection of records that are kept regarding economic transactions between the various tiers? Should the enforcement staff be increased in order to permit these inspections?

7. Can the price posting system be simplified, expedited, or enforced in more appropriate ways?

For example, should information in the price posting system be accessible to everyone electronically?

Should all agreements associated with details of posted prices also be made available to the general public and, therefore, available for examination by all retailers and distributors?

What investments should be made in order to shorten the time it takes to bring a new product into Washington markets?

8. How should Internet sales be regulated?

Should a permit be required for the delivery of alcohol to private address? Should such a permit be tied to the delivery of products that have been furnished to the delivery agency through a licensed wholesaler? Under these circumstances, should the wholesaler be responsible for the collection of Washington State taxes?

Should the state of Washington establish a policy that the delivery of alcohol to an address within the state implies that the purchase of the alcohol took place within the borders of the state – i.e., at the address of the purchaser?

What is the status of the review panel?

Questions one through four have been reviewed and discussed by the panel. The following, proposed language, previously drafted as a possible addition to RCW 66.28.010 by the Washington State Liquor Control Board's former legal counsel, Assistant Attorney General Kim O'Neal, was used as a base for discussions:

"Unless the board reviews the ownership and proposed methods of operation of all involved entities and determines that there will not be an unacceptable level of control or undue influence over the operation of the retail licensee or unless the board determines that the ownership interest which would otherwise be a violation of this section is *de minimus* pursuant to regulations promulgated by the Board."

Several alternative drafts of proposed amendments to Washington's Tied House law have been proposed by individual panel members. A subcommittee of this panel will meet on September 3, 1999, to hopefully come to consensus on language. This language will then be reviewed by the full panel. Our goal is to present these proposed changes to the Liquor Control Board Members by mid September.

The panel will examine the remaining issues (questions six through eight), and decide if they can reasonably reach consensus on any of the issues. If so, the panel will continue to meet to discuss these points.

attachments

Three Tier System Review Panel

Why conduct a review of the three tier system?

Washington State's system for the post-Prohibition regulation of alcohol was set in place by the legislature in 1934 in the Steel Act, which both legalized the sale of alcohol and established a three tier system separating manufacturing, wholesaling, and retailing from one another. This basic structure still forms the "backbone" of the licensing and regulation structure.

The complexity of corporate organization has increased considerably since 1934, due especially to the emergence of the multi-purpose corporation which owns and operates a variety of disparate enterprises. Every recent legislative session has considered proposals intended to make exceptions to the three tier system, many of which have been enacted. The changing business atmosphere coupled with the growing impact of electronic technologies will continue to bring challenges to this policy.

For these reasons, the Washington State Liquor Control Board will be conducting a review of the three tier system. The recommendations from this review will be available for consideration in the legislature that will convene in the year 2000.

What is the role of the advisory panel?

To assist the Liquor Control Board in the formulation of recommendations and in order to provide for an open, informed debate, the Board is convening an advisory panel that will include members representing the groups listed below. Wherever an association represents these interests, the appropriate association will be asked to name the representatives.

Manufacturers (3)

Retailers (2)

Licensed Beverage Association

Legislators (4)

Beer and Wine Distributors (2)

Restaurant Association of Washington

General Interest (3)

The panel will be asked to formulate recommendations in the following three areas:

1. Should legislation be considered that would better accommodate the three tier structure to the contemporary corporate world?
2. What changes, if any, should be made to simplify the rules and regulations of the Washington State Liquor Control Board associated with the three tier system? How can the expense and time involved in the regulation of these separate tiers be reduced?
3. Are there any changes in three tier system associated law or rule that should be considered because of the impact of emerging new technologies on the structures of corporations or on other business practices? Are there changes in state rule or law that should be considered given the emergence of electronic retailing systems that cross state and national boundaries?

Meetings...

The panel will meet on November 19, 1998, December 10, 1998, January 25, 1999 and March 22, 1999 in Olympia; and then bi-monthly from May through July of 1999.